

II. ESTATE TAX REPEAL

Individuals who contemplate relinquishing citizenship or terminating residency for tax purposes generally consider three main U.S. taxes: the income tax, the estate tax, and the gift tax. For some taxpayers, the estate tax (the maximum rate of which reaches 49 percent for 2003) may serve as the principal motivating factor in the decision to relinquish citizenship or terminate residency.

In view of the small number of expatriating individuals relative to the overall number of persons potentially subject to the U.S. estate tax, this study cannot definitively establish a causal link between the estate tax and citizenship relinquishment or residency termination. However, the Joint Committee staff observes from a review of individual cases that several of the individuals who have relinquished citizenship or terminated residency have substantially reduced their potential worldwide estate tax liability by doing so. This experience suggests that a general analysis of tax-motivated citizenship relinquishment or residency termination and the rules that address these situations must be premised, in part, on the existence of an estate tax that, absent special rules, might be avoided by relinquishing citizenship or terminating residency. Recent developments in the law, however, may call this premise into question and thus affect this analysis.

EGTRRA made a number of changes to the estate and gift tax rules, including incremental rate reductions and unified credit increases from 2002 to 2009, and repeal of the estate tax for estates of decedents dying after December 31, 2009. However, EGTRRA also included a “sunset” provision, pursuant to which EGTRRA’s provisions, including estate tax repeal, do not apply to estates of decedents dying after December 31, 2010. Thus, under present law, the estate tax phases down from 2002 to 2009, is repealed for 2010, and then is reinstated in 2011, without the rate reductions and unified credit increases that were phased in prior to repeal.

In the 107th Congress, several bills were introduced that would make estate tax repeal permanent (e.g., H.R. 586, H.R. 2143, H.R. 2316, H.R. 2327, and H.R. 2599) and one bill was introduced to accelerate estate tax repeal (S.3). The House passed H.R. 586 and H.R. 2143. In addition, the Senate passed, as Senate Amendment 2850 to S. 1731 (an agriculture reauthorization bill), a provision expressing the Sense of the Senate that estate tax repeal should be made permanent. The House also passed a similar measure (H. Res. 524). The Senate did not pass a bill making estate tax repeal permanent.

The analysis and recommendations in this report are based on present law, including the relevant changes made by EGTRRA, and no attempt is made to predict how the law might be amended in the future. Under present law, an estate tax is imposed on large estates in every year except one (2010), with a top marginal rate ranging from 45 percent to 55 percent, and the concern remains that this tax may be avoided in whole or in part by means of citizenship relinquishment or residency termination. Thus, despite the possibility of eventual permanent repeal of the estate tax, this report is premised on the present-law estate tax, the possibility of its avoidance by means of citizenship relinquishment or residency termination, and the goal of mitigating such avoidance.

If estate tax repeal were made permanent, then much of the analysis contained in this report would need to be revisited. For example, the incidence of tax-motivated citizenship relinquishment and residency termination likely would decline to some extent, since estate tax avoidance would be largely eliminated as a motivating factor.¹⁹ Nevertheless, income tax avoidance, and perhaps gift tax avoidance, would remain motivating factors in some instances. The recommendations set forth in this report might need to be reevaluated if the tax incentives for expatriating or terminating residency were reduced, and were limited to income and gift tax avoidance. The potential impact of permanent estate tax repeal on the analysis and recommendations is noted as appropriate throughout the report.

¹⁹ It might not be entirely eliminated, to the extent that revival of the tax were perceived as a possibility.